

Message Text

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UNCLAS STATE 291880 TOSEC 310330

FOR UNDER SECRETARY ROGERS FROM SORENSON

FOLLOWING REPEAT CANBERRA 8583 ACTION SECSTATE INFO OECD PARIS
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QUOTE

UNCLAS CANBERRA 8583

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SUBJ: GOA TREASURER'S DEVALUATION ANNOUNCEMENT

1. FOLLOWING IS THE TEXT OF THE STATEMENT MADE NOVEMBER 28
IN MELBOURNE BY GOA TREASURER LYNCH ANNOUNCING THE 17 1/2
PERCENT DEVALUATION OF THE AUSTRALIAN DOLLAR TOGETHER WITH
NUMEROUS ACCOMPANYING FINANCIAL MEASURES. EMBASSY COMMENTS
ON DEVALUATION DEVELOPMENTS FOLLOW SEPTTEL.

2. QUOTE THE TREASURER, MR. PHILLIP LYNCH, ANNOUNCED
TODAY THAT THE AUSTRALIAN DOLLAR WOULD BE DEVALUED BY 17 1/2
PERCENT WITH EFFECT FROM THE OPENING OF BUSINESS TOMORROW
MORNING.

THE DEVALUATION WILL BE ACCOMPANIED BY A NUMBER OF POLICY
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MEASURES DESIGNED BOTH TO MAXIMIZE THE BENEFICIAL EFFECTS
OF THE MOVE AND TO OFFSET PRICE AND MONETARY EFFECTS THAT
WOULD OTHERWISE RUN COUNTER TO THE GOVERNMENT'S ANTI-
INFLATIONARY STRATEGY.

THE TREASURER SAID THAT AS WELL AS THE INITIAL CHANGE IN THE EXCHANGE RATE TO A NEW LEVEL (\$A1 EQUALS \$US1.0174) WHICH WOULD GIVE EFFECT TO THE DEVALUATION, A CHANGED PATTERN OF MANAGEMENT OF THE EXCHANGE RATE WOULD HENCEFORTH BE ADOPTED.

THE CHANGED ARRANGEMENTS WOULD COMPRISE A VARIABLE LINK TO A TRADE-WEIGHTED 'BASKET' OF CURRENCIES.

THE AUSTRALIAN DOLLAR HAD SINCE SEPTEMBER 1974 REMAINED PEGGED IN A FIXED RELATIONSHIP TO THE AVERAGE OF A TRADE-WEIGHTED 'BASKET' OF CURRENCIES.

THE PEGGIN OF THE RATE FOR LENGTHY PERIODS WAS NOW DISCONTINUED; THE LEVEL OF THE EXCHANGE RATE IN RELATION TO THE 'BASKET' OF CURRENCIES WILL BE KEPT UNDER REVIEW, AND THE GOVERNMENT WOULD, IN EFFECT, BE ADOPTING A FLEXIBLY ADMINISTERED RATE, SOMEWHAT ALONG THE LINES OF A MANAGED FLOAT.

WHEN THE ASSESSMENT OF ALL RELEVANT ECONOMIC FACTORS INDICATED A NEED FOR MOVEMENT IN THE LEVEL OF THE EXCHANGE RATE, THIS WOULD TAKE PLACE BY MEANS OF MORE FREQUENT AND SMALLER SHIFTS IN THE RELATIONSHIP OF THE AUSTRALIAN DOLLARS TO THE 'BASKET' OF CURRENCIES.

THE TREASURER WILL BE RESPONSIBLE FOR THESE ARRANGEMENTS.

THE GOVERNOR OF THE RESERVE BANK, WITH THE SECRETARY OF THE TREASURY AND THE SECRETARY OF THE DEPARTMENT OF THE PRIME MINISTER AND CABINET, WOULD COMPRISE THE GROUP WHICH KEEPS THE LEVEL OF THE EXCHANGE RATE UNDER REVIEW.

THE TREASURER SAID THAT THE ARRANGEMENT WAS AN APPROPRIATE RESPONSE TO THE CHANGING NATURE OF ECONOMIC CONDITIONS ABROAD AND OF AUSTRALIA'S INTERNATIONAL TRADING RELATIONSHIPS; THE ARRANGEMENT WAS DESIGNED TO AVOID THE BUILDING-UP FOR THE UNCLASSIFIED

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FUTURE OF EXPECTATIONS OF MAJOR SHIFTS AT LONG INTERVALS IN THE EXCHANGE RATE.

THE CHANGED SYSTEM WOULD PERMIT THE USE OF THE EXCHANGE RATE, BY MEANS OF CHANGES UPWARDS OR DOWNWARDS IN THE RATE AS APPROPRIATE, AS A MORE FLEXIBLE ELEMENT AMONGST THE AVAILABLE ARMS OF ECONOMIC POLICY.

THE GOVERNMENT HAD BEEN FORCED TO DEVALUE, MR. LYNCH SAID, BECAUSE OF THE DETERIORATION THAT HAD OCCURRED OVER RECENT YEARS IN AUSTRALIA'S UNDERLYING EXTERNAL SITUATION, AS A RESULT OF THE HIGHER INCREASE IN WAGE COSTS THAN IN OUR MAJOR TRADING PARTNERS AND THE CONTINUING LOSS OF RESERVES.

THE TREASURER SAID THAT ECONOMIC DEVELOPMENTS, PARTICULARLY THE DISPARITY IN OVERSEAS COSTS COMPARED WITH OTHER COUNTRIES, COULD HAVE JUSTIFIED A VARIATION IN THE EXCHANGE RATE EARLIER THIS YEAR.

HOWEVER, THE GOVERNMENT DECIDED, AS PART OF ITS ANTI-INFLATION STRATEGY, NOT TO TAKE ANY ACTION AT THAT TIME.

IT NOW CONSIDERED THAT VARIOUS SECTORS OF THE ECONOMY, PARTICULARLY THE MANUFACTURING AND PRIMARY INDUSTRIES, WERE BEING FORCED TO BEAR AN UNDUE AND INDEED UNFAIR BURDEN WHICH SHOULD BE RELIEVED TO SOME EXTENT BY THIS PRESENT ACTION.

THIS ADJUSTMENT OF THE RATE WOULD INSTILL CONFIDENCE IN BOTH THESE ECONOMIC SECTORS LEADING TO GREATER ACTIVITY AND MORE EMPLOYMENT.

INDEED THE PRODUCTIVE SECTORS OF THE AUSTRALIAN ECONOMY, THE MANUFACTURING, MINING AND OTHER PRIMARY INDUSTRIES, SHOULD ALL TAKE HEART FROM THIS DECISION.

PARTICULARLY AGAINST THE BACKGROUND OF THE OBVIOUS RELUCTANCE OF THE CONCILIATION AND ARBITRATION COMMISSION TO RECOGNIZE THE NEED TO AWARD LOWER INCREASES IN WAGES, HIGHLIGHTED BY THE RECENT DECISION TO PASS ON THE WHOLE OF THE SEPTEMBER QUARTER CONSUMER PRICE INCREASE, IT HAD BECOME INCREASINGLY CLEAR THAT THERE WAS LITTLE OR NO CHANCE OF RESTORING UNCLASSIFIED

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COMPETITIVENESS OF AUSTRALIAN INDUSTRIES BY PURELY DOMESTIC POLICIES.

THE GOVERNMENT COULD NOT HAVE ALLOWED THE SITUATION TO CONTINUE IN AN ATMOSPHERE OF INCREASING UNCERTAINTY, IN THE HOPE THAT UNDERLYING COST DISABILITIES SUFFERED BY AUSTRALIAN INDUSTRIES WOULD EVENTUALLY BE CORRECTED.

THAT WOULD HAVE IMPOSED TOO HEAVY A BURDEN ON EXTERNAL POLICY AND HAVE PUT AT RISK AUSTRALIA'S EXPORT AND IMPORT COMPETING INDUSTRIES.

RECENT MINING DIFFICULTIES, THE DISASTROUS FALL IN RURAL INCOMES AND THE INCREASING MOVEMENT OF AUSTRALIAN MANUFACTURING OFFSHORE DEMONSTRATED THE NEED FOR ACTION.

RURAL INCOMES, FOR EXAMPLE, HAD FALLEN BY NO LESS THAN 65 PERCENT IN REAL TERMS OVER THE PERIOD FROM 1973/74 TO 1975/76.

MOREOVER, THERE HAD BEEN AN INCREASING LOSS OF INTERNATIONAL RESERVES IN RECENT MONTHS AS INTERNATIONAL TRADERS AND INVESTORS INCREASINGLY FIRMED THEIR ASSESSMENTS THAT THERE

WOULD BE A DEVALUATION, HOLDING BACK INVESTMENT IN AUSTRALIA AND TAKING OTHER ACTION TO PROTECT THEIR POSITIONS.

AUSTRALIA'S INTERNATIONAL RESERVES HAD FALLEN BY MORE THAN \$1,000 MILLION OVER THE LAST TWELVE MONTHS, NOTWITHSTANDING THE RESUMPTION OF OVERSEAS BORROWINGS BY THE GOVERNMENT. THE RATE OF LOSS OF RESERVES HAD INCREASED SIGNIFICANTLY IN RECENT MONTHS, WITH A FALL OF \$600 MILLION SINCE END JULY DESPITE \$240 MILLION OVERSEAS BORROWINGS BY THE GOVERNMENT IN THAT PERIOD.

IN OCTOBER RESERVES DECLINED BY \$269 MILLION; IN NOVEMBER TO DATE THERE HAD BEEN A FURTHER FALL OF APPROXIMATELY \$260 MILLION.

THIS DECLINE IN RESERVES HAD CONTINUED DESPITE THE ADDITIONAL MONETARY MEASURES ANNOUNCED ON 7 NOVEMBER AND HAD LEFT OFFICIAL RESERVES AT 26 NOVEMBER AT AROUND \$2,100 MILLION, SUFFICIENT TO COVER LESS THAN THREE MONTHS' IMPORTS.

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ADDED TO THAT THE GOVERNMENT FACED THE PROSPECT OF AN EVEN GREATER RATE OF OUTFLOW AROUND THE END DECEMBER/EARLY JANUARY PERIOD.

TO HAVE ALLOWED THE SITUATION TO DETERIORATE FURTHER WOULD HAVE BEEN TO ADMIT THE POSSIBILITY OF ENORMOUS SPECULATIVE GAINS, WITH CONSEQUENT COSTS TO THE AUTHORITIES.

IN THE LIGHT OF ITS ASSESSMENT OF THE SITUATION, INCLUDING ITS ASSESSMENT OF ATTITUDES IN FINANCIAL MARKETS IN AUSTRALIA AND OVERSEAS, THE GOVERNMENT HAD THEREFORE CONCLUDED THAT THERE WAS NO ALTERNATIVE BUT TAKE EARLY DECISIVE ACTION.

THE GOVERNMENT'S DECISION, MR. LYNCH SAID, WOULD BE OF ENORMOUS BENEFIT IN HELPING TO RESTORE THE VIABILITY OF AUSTRALIA'S EXPORT INDUSTRIES, SUCH AS THE RURAL AND MINING INDUSTRIES AND MANUFACTURING EXPORTERS, AS WELL AS THOSE SECTORS OF INDUSTRY EXPERIENCING UNDUE PRESSURE FROM IMPORT COMPETITION.

A MAJOR ADVANTAGE THAT WOULD ACCRUE FROM THE PACKAGE WOULD BE A RESUMPTION IN THE INFLOW OF LONG-TERM INVESTMENT CAPITAL.

THE FOREIGN INVESTMENT REVIEW BOARD HAD APPROVED A SUBSTANTIAL NUMBER OF MAJOR DEVELOPMENT PROJECTS IN RECENT TIMES, BUT UNCERTAINTY ABOUT THE EXCHANGE RATE HAD DELAYED THEIR INITIATION.

TODAY'S DECISION WOULD ALLOW THESE PROJECTS TO GO AHEAD AND WOULD, AS A CONSEQUENCE, UNDERWRITE AND SUPPORT ECONOMIC

RECOVERY.

THE GOVERNMENT'S DECISION IN NO WAY MEANT THAT THE BASIC ANTI-INFLATIONARY STRATEGY HAD CHANGED, THE TREASURER SAID.

WHILE THERE WOULD BE SOME INCREASES IN DOMESTIC PRICES AND COSTS AS A RESULT OF THE MOVE, THE GOVERNMENT'S PRIMARY OBJECTIVE REMAINED TO BRING INFLATION UNDER CONTROL.

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THE GOVERNMENT BELIEVED THAT RECOVERY IN ECONOMIC ACTIVITY AND EMPLOYMENT OVER THE ECONOMY AS A WHOLE WOULD HAVE TO BE GRADUAL IF THE RECOVERY WAS TO BE SUSTAINED.

THE TREASURER SAID THAT WITHIN THE FRAMEWORK OF THIS GENERAL APPROACH TO ECONOMIC POLICY, ACTION THAT WAS BEING TAKEN TO REDUCE THE BURDEN AS EXTERNAL POLICY CLEARLY MADE NECESSARY A FIRMING OF THE VARIOUS ARMS OF DOMESTIC POLICY.

ACTION WAS PROPOSED ON THE FISCAL, MONETARY AND WAGES FRONTS.

ACTION ON THE MONETARY FRONT WAS PARTICULARLY NECESSARY TO ENSURE THAT THE DEVALUATION WAS NOT REFLECTED IN ANY EASING OF CONDITIONS IN PRIVATE CAPITAL MARKETS.

FOR THIS REASON THE GOVERNMENT HAD DECIDED ON A FURTHER INCREASE IN OFFICIAL INTEREST RATES.

THERE WOULD ALSO BE A CLOSE MONITORING OF THE VOLUME OF LENDING BY THE VARIOUS FINANCIAL INSTITUTIONS TO ENSURE THAT THE GROWTH IN LENDING CAME BACK FROM RECENT EXCESSIVE AND UNSUSTAINABLE LEVELS TO A PACE CONSISTENT WITH THE SOUND DEVELOPMENT OF THE ECONOMY.

THE TREASURER SAID THAT HE HAD INDICATED A NEED FOR THIS EARLIER IN THE MONTH.

THE CHANGE IN THE EXCHANGE RATE PUT ADDED EMPHASIS ON THE NEED FOR AN EARLY SLOWING IN THE PACE OF LENDING BY THE VARIOUS INTERMEDIARIES.

WITH REGARD TO OFFICIAL INTEREST RATES THE TREASURER SAID THERE WOULD BE AN INCREASE IN THE YIELD ON TREASURY NOTES AS FROM THE COMMENCEMENT OF BUSINESS ON MONDAY 29 NOVEMBER.

THE ISSUE PRICE FOR 13 WEEK NOTES WILL BE 97.81 PERCENT AND THE YIELD TO MATURITY WILL BE INCREASED FROM 8.478 PERCENT TO 8.981.

THIS ISSUE PRICE FOR 26 WEEK NOTES WILL BE 95.60 PERCENT AND THE YIELD TO MATURITY WILL BE INCREASED FROM 8.727 PERCENT

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TO 9.230 PERCENT.

AN ADJUSTMENT OF SIMILAR MAGNITUDE WILL BE MADE IN YIELDS ON SHORT-DATED BONDS, WITH CONSEQUENTIAL ADJUSTMENT ON A DIMINISHING BASIS, OF YIELDS ON OTHER SECURITIES.

THE MONETARY AUTHORITIES WILL BE TAKING ACTION DURING THE COURSE OF THE COMING WEEK DIRECTED TOWARDS HAVING THE NEW YIELD STRUCTURE ESTABLISHED PROMPTLY.

THE TREASURER SAID THAT, NOTWITHSTANDING TODAY'S DECISION, A PERIOD OF TIGHTNESS IN LIQUIDITY COULD BE EXPECTED IN THE JUNE QUARTER 1977, AND ENTERPRISES SHOULD PLAN ACCORDINGLY.

THERE SHOULD BE NO EXPECTATION THAT MONETARY POLICY WOULD BE EASED TO ACCOMMODATE DEMANDS FOR FUNDS AT THAT TIME FROM THOSE WHO HAD ACTED WITHOUT DUE PRUDENCE.

TURNING TO FISCAL POLICY, THE TREASURER NOTED THAT THE 1976/77 BUDGET HAD CUT BY HALF THE RATE OF INCREASE IN OUTLAYS AS COMPARED WITH THE OUTCOME FROM THE PREVIOUS YEAR.

AS HE HAD STRESSED ON SEVERAL OCCASIONS, THE GOVERNMENT WAS COMMITTED TO KEEPING WITHIN THAT BUDGET TOTAL.

AS PART OF THE NECESSARY TIGHTENING OF DOMESTIC POLICIES, HOWEVER, A REVIEW OF EXPENDITURES WAS BEING PUT IN HAND IMMEDIATELY.

THIS REVIEW WOULD IDENTIFY AREAS WHERE FURTHER SAVINGS COULD BE MADE BY THE DEFERMENT OF EXPENDITURES UNTIL LATER IN THIS FINANCIAL YEAR OR INTO 1977/78.

THE TREASURER ALSO NOTED THAT MINISTERS AND THEIR DEPARTMENTS ARE CURRENTLY PREPARING THEIR FORWARD ESTIMATES OF EXPENDITURE FOR THE NEXT THREE YEARS IN THE KNOWLEDGE THAT THE GOVERNMENT FACES A LONG HAUL IN RESTORING A BETTER BALANCE BETWEEN THE PUBLIC AND PRIVATE SECTORS.

MINISTERS, ACTING BOTH INDIVIDUALLY AND COLLECTIVELY, WILL BE IDENTIFYING FURTHER REDUCTIONS IN THEIR EXISTING PROGRAMS.

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IN ADDITION, ANY INCREASES ABOVE THE REAL LEVELS OF OUTLAYS IN THE CURRENT FISCAL YEAR IN RELATION TO WHICH THERE IS NOT AN ALREADY-EXISTING FIRM COMMITMENT, WILL BE TREATED AS NEW PROPOSALS.

IN PUTTING THESE FORWARD, THE UTMOST RESTRAINT AND SELF-DISCIPLINE WILL BE EXERCISED, NO MATTER WHAT THE INTRINSIC MERITS OF THE PROPOSALS MIGHT APPEAR TO BE.

THE TREASURER SAID THAT THE WAGES FRONT ASSUMED ESPECIAL IMPORTANCE IN THE PRESENT CONTEXT.

THE DECISION BY THE CONCILIATION AND ARBITRATION COMMISSION TO FULLY INDEX THE INCREASE IN THE SEPTEMBER QUARTER CONSUMER PRICE INDEX INTO WAGES HAD BEEN TOTALLY AT ODDS WITH THE WHOLE THRUST OF GOVERNMENT POLICY.

THAT DECISION HAD DEALT A BLOW TO HOPES FOR A CONTINUED DE-ESCALATION OF PRICE INCREASES AND AN EARLY DECLINE IN UNEMPLOYMENT.

IT HAD ALSO CONTRIBUTED TO THE EXCESSIVE BURDEN BEING PUT ON EXTERNAL POLICY WITHIN THE TOTAL POLICY FRAMEWORK.

TO HAVE ALLOWED THIS TO CONTINUE WOULD HAVE BEEN QUITE UNFAIR TO EXPORT AND IMPORT COMPETING INDUSTRIES.

A SUBSTANTIAL TIGHTENING OF WAGE POLICY HAD TO BE ACHIEVED IF PROGRESS TOWARDS NATIONAL ECONOMIC GOALS WAS TO BE MAINTAINED.

THE COMMONWEALTH WOULD BE ARGUING, IN THE STRONGEST POSSIBLE TERMS, FOR RESTRAINT IN THE DECEMBER QUARTER NATIONAL WAGE CASE.

LOOKING BEYOND THAT, THE GOVERNMENT WAS STRONGLY OF THE BELIEF THAT DEVALUATION SHOULD NOT LEAD TO ANY ESCALATION OF THE RATE OF INCREASE IN WAGE SETTLEMENTS.

TO ALLOW THIS TO HAPPEN WOULD BE TO NEGATE THE BENEFICIAL UNCLASSIFIED

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EFFECTS THAT WERE BEING SOUGHT FOR THE COMPETITIVE POSITION OF AUSTRALIAN INDUSTRY AND THE RESTORATION OF CONFIDENCE IN THE ECONOMIC FUTURE.

THE GOVERNMENT WOULD THEREFORE BE DOING EVERYTHING IN ITS POWER TO ENSURE THAT ANY IDENTIFIABLE EFFECTS OF THE DEVALUATION DECISION UPON THE CONSUMER PRICE INDEX DID NOT FLOW ON INTO WAGES, EITHER THROUGH NATIONAL WAGE CASE HEARINGS OR MORE GENERALLY.

TAKEN AS A WHOLE THE GOVERNMENT'S PRESENT ACTION SHOULD GIVE FULL CONFIDENCE TO THE COMMUNITY THAT WE ARE FIRMLY ON THE PATH TOWARDS RESTORATION OF THE NATION'S FULL ECONOMIC HEALTH. END QUOTE.
HARGROVE

UNQUOTE ROBINSON.

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